

Perfection in relation to creditor extinction in manufacturing contracts



University of Oslo
Faculty of Law

Candidate number: 5008

Supervisor: Erik Røsæg

Deadline for submission: 01.11.2010

Number of words: 17,830 (max. 18.000)

28.10.2010

Content

<u>1</u>	<u>INTRODUCTION</u>	<u>1</u>
1.1	The main problem	1
1.2	Aim of the thesis	1
1.3	The conflict situations	2
1.4	Property	3
1.5	The starting point in creditor extinction	4
1.6	Considerations of creditor extinction	5
1.7	Structure of the thesis	8
<u>2</u>	<u>CREDITOR PROTECTION IN MANUFACTURING CONTRACTS</u>	<u>9</u>
2.1	Overview	9
2.2	Creditor protection in NSF 2000	10
2.3	Creditor protection in NF 05	13
<u>3</u>	<u>CREDITOR PROTECTION BY WAY OF REGISTRATION</u>	<u>15</u>
3.1	Introduction	15
3.1.1	Overview	15
3.1.2	The different types of legal registers	16
3.1.3	Justification of registration of rights in property registers	17
3.2	The ship registers (NOR/NIS)	18
3.2.1	Overview	18
3.2.2	The ship building register	19

3.3	Perfection	20
3.3.1	Introduction	20
3.3.2	What can be registered	21
3.3.3	The material perfection rules	22
4	<u>PERFECTION IF THE CONTRACT/CONTRACTUAL OBJECT IS NOT REGISTERED</u>	28
4.1	Introduction	28
4.2	Whether the perfection rules for chattels is applicable if the contract is not registered	29
4.2.1	Introduction	29
4.2.2	Is the buyer's non-registered right in the contractual object in reality a security interest?	30
4.2.3	Generally, whether the perfection rules for chattels is applicable in the situation where registration option has not been used	33
5	<u>CREDITOR PROTECTION REGARDING CHATTELS</u>	36
5.1	Introduction	36
5.1.1	Security for the buyers claim – Legal protection by agreement or handover?	36
5.2	Perfection regarding chattels	38
5.2.1	The main rule	38
5.2.2	The core of the problem	38
5.3	Perfection without handover	38
5.3.1	General regarding perfection, with basis in case law	38
5.3.2	The interest doctrine	40
5.3.3	Justification for departing from the requirement of handover	40
5.3.4	Exemption from the handover doctrine in consumer contracts	42
5.4	The exemption from the requirement of handover in manufacturing contracts	44
5.4.1	The special features of manufacturing contracts	44
5.4.2	The exemption from the requirement of handover for manufacturing contracts	45
5.4.3	Whether the exemption for manufacturing contracts extends to materials, parts and equipment	49

5.5 The situation where neither payment or handover have taken place at the time of the bankruptcy/creditor seizure	54
<u>6 CONCLUSION</u>	<u>55</u>
<u>REFERENCES</u>	<u>58</u>

1 Introduction

1.1 The main problem

A is building a ship for B. There is a written contract, it is however not registered and neither is the contractual object. When the construction is 97% completed A, which have struggled to handle his incoming claims declare bankruptcy.

The question is whether B has perfection for his right in the newbuilding, in relation to the yard's creditors, and thereby a separatist right in the contractual object.

This question was the core of the Bomek-case¹, and is also the problem addressed in this thesis. However in order to answer it, one must first question whether the perfection rules for chattels may be applied, when the option to register the contract/contractual object according to MC § 31 have not been used. Secondly, one must question whether there is an exemption for manufacturing contracts from the requirement of handover to obtain perfection regarding chattels. In order to illustrate the importance of the problem, I will also discuss the particular features of bankruptcy protection in large manufacturing contracts, (NF 05 and NSF 2000) and the perfection rules in relation to creditor extinction if the contract is registered.

1.2 Aim of the thesis

¹ ND.1982.264.Bodø Namsrett.

In large manufacturing contracts there are large amounts of money involved. This urges a system of clear-cut rules in which the parties in these contracts easily may predict their legal position and secure their interests. The registration option in MC § 31, and especially the legal position if the option has not been used constitutes an uncertain element in an otherwise predictable system of rules. The specific objective of the thesis is to assess the state of the law if the registration option has not been used. In order to do so I will consider the characteristics of the manufacturing contracts, the state of the law if the registration option has been used, and the perfection rules for chattels. Through such a wide discussion I will be able to assess the main problem as a part of the system of property law.

1.3 The conflict situations

Creditor extinction is categorized as a part of property law, which is about the creation, extinction and transfer of rights². Regarding transfer of rights in real property or chattels conflicts regarding incompatible rights may occur. These are known as priority conflicts, and may be divided into two groups. The first conflict is when two or more parties have acquired incompatible rights to an asset from the same person. This is referred to as a conflict of double conveyance. In a bankruptcy situation where there is conflict regarding rights in an asset, the parties in the priority conflict are the buyer and the bankruptcy estate. In relation to the bankruptcy estate it is common to say that the asset is on its way out of the estate. Secondly, conflict can occur between the acquirer and the rightful owner, where the rightful owner claims that the seller lacked the necessary right of disposition in relation to the asset. This is a rightful owners conflict, between the rightful owner and the acquirer's estate. In relation to the acquirer's bankruptcy estate, the asset is entering the estate.

Creditor extinction can occur in the form of a creditor seizure, or bankruptcy proceedings, (bankruptcy or compulsory composition). The rules regarding creditor extinction in a

² Brækhus. Tingsrett S.371

creditor seizure and bankruptcy are usually similar. However there are differences, especially in relation to rights that can be registered in a property register³.

1.4 Property

The owner of an asset has actual and legal right to disposition over the asset in question. The actual right of disposition involves that the owner may use the asset in whichever way he would like, and deny others the right to do the same. The owner's legal right of disposition allows the owner to dispose over the asset, for instance by giving it away, leasing or selling it. The owners right of disposition is not unlimited, but depends on what remedies are allowed according to the framework of national legislation. The owners right of disposition is considered to be all kinds of dispositions that the framework of national legislation have not explicitly bounded against⁴. In other words property rights are negatively defined⁵. The owners right of disposition is also limited by other parties positively limited rights in the asset. The property right in a certain case is the negatively defined sum of dispositions the owner has at his disposal⁶.

In Norwegian law we have freedom of contract within the framework of mandatory legislation. The framework follows from statutory rules in the conclusion of agreements act, the satisfaction of claims act, the mortgage act, the maritime code, the property registration act, and so on. Further there is also non-statutory law, which is based on case law, theory, customs and so on. An example is the perfection rules for chattels. It is important to emphasize that non-statutory law also can be mandatory. For instance the rules regarding creditor protection are mandatory in relation to third party creditors⁷. Resulting in

³ Compare MC §23 and §25.

⁴ Brækhus. Tingsrett S.15

⁵ Brækhus. Tingsrett S.15

⁶ Brækhus. Tingsrett S.15

⁷ Lilleholt. S.198.

that parties to a contract cannot agree on terms that weaken the third party creditors position.

1.5 The starting point in creditor extinction

The main rule for the creditors right to coverage in Norwegian law follows from the Norwegian Satisfaction of Claims Act 1984. § 2-2⁸. “Unless otherwise provided by law or other valid provision, the creditor is entitled to coverage in any assets belonging to the debtor at the time of seizure, which can be sold rented or in other ways be converted into money”. In other words the starting point is that the creditors cannot obtain a better right in an asset than the debtor had⁹. However, there are important exemptions from this principle. In several situations the creditor seizure can surpass older rights in the asset in question. This is called creditor extinction, and is justified by the consideration to avoid creditor fraud¹⁰.

In a conflict between a younger creditor seizure and an older right in the asset, the older right must be perfected to be recognized and hence not extinguished. Perfection in regard to creditor extinction can be obtained in three different ways depending on the nature of the asset; through registration, deprivation of possession, and notification, (with the exemption of the Mortgage Act § 3-17.1) The specific rules regarding perfection will be reviewed later in the thesis¹¹.

SCA § 2-2 as the general legal basis for any creditor seizure extensively limits the creditors possibility to take cover in the debtor’s assets. “The assets have to belong to the debtor at the time of the seizure”¹². Right to take cover beyond SCA § 2-2 requires authority in

⁸ The Satisfaction of Claims Act will later in the thesis be known only as SCA.

⁹ Andenæs.Konkurs.S.48.

¹⁰ Lilleholt. S.169.

¹¹ Exempt for rules regarding legal protection trough notification. These will not be reviewed in the thesis.

¹² SCA § 2-2

“statute or other valid provision”¹³. “Other valid provision” also comprise exemptions from the creditors right to cover in non-statutory law. Firstly, the wording indicates that the assets have to actually belong to the debtor, and thereby excludes assets the debtor has sold or has leased and so on. The estate cannot get a better right in the asset than the debtor had. Since there is no valid provision for exemption, the estate cannot extinguish a rightful owner’s (H) right in an asset that have been transferred to the debtor A pro forma¹⁴. As a consequence actual creditor extinction is limited to conflicts of double conveyance, (the conflict S-B). However, it must be emphasized that there can be a conflict between the creditor (B) and the rightful owner (H). In a transaction of real estate from H to A, a creditor B can extinguish the rightful owner’s H cancellation disclaimer, if the disclaimer has not been registered at the time of the creditor seizure/bankruptcy¹⁵. This problem will not be reviewed any further in this thesis. Secondly, there is a limitation in time. The asset must belong to the debtor at the time of the seizure.

Further it is a condition in order to take cover in an asset that it “can be sold rented out, or in another way be converted into money”. This is a natural limitation as the purpose of bankruptcy is to turn the debtors assets into money, and split it between the creditors.

1.6 Considerations of creditor extinction

Creditor extinction is an exemption from SCA § 2-2 and is when a younger creditor seizure supersedes an older right in an asset¹⁶. Norwegian property law consists of a complex system of rules. In order to really understand these rules, the key lies in recognizing the underlying system. To see this system one must view the rules in light of words of art¹⁷ that scholars have introduced in legal theory. Together these words of art express a legal

¹³ SCA § 2-2

¹⁴ Rt.1935.981 (Bygland)

¹⁵ For a more thorough presentation see: Lilleholt. (JV-1996-69.s.91)

¹⁶ Lilleholt. (JV-1996-69 s. 70)

¹⁷ Norwegian: Begrep

principal with fundamental weight. However one must keep in mind that the Norwegian law has a thorough tradition for skepticism in the use of words of art. According to Norwegian law one cannot base the result of legal reasoning merely on words of art. This is because words of art are not interpreted equally in the different areas of law. For instance *appearance* is not interpreted equally in penal law and property law¹⁸. Legal reasoning based merely on words of art is known as jurisprudence of concepts and can easily result in circular argumentation. So if one must use words of art, as Arnholm said - “one should put them in quotes, which shall show that one really does not mean anything by the word and at least nothing wrong”¹⁹. As a consequence conclusions should never be drawn from words of art²⁰.

These words of art are *appearance*, *publicity* and *evidence*²¹. In property law *appearance* usually means “an outer reflection of right that someone appears to be the correct person concerned to dispose legally”²². In this context the *appearance* may completely correspond to the disposer’s right, but it can also differ. *Publicity* means “that something is more or less available for insight from others”²³, while *evidence* usually means “that something is verifiable, or that it can be controlled”²⁴. To further describe the content of the words of art one must consider the specific rules. There the words of art work as a guideline in the system of rules.

The main justification for the rules of creditor extinction is to prevent creditor fraud. Traditionally²⁵, it has been discovered that when someone faces bankruptcy there are quite a few people the debtor wants to favor rather than his creditors. As a consequence any

¹⁸ Norsk: Legitimasjon.

¹⁹ Arnholm. S.31.

²⁰ Lilleholt.(JV-1996-69)

²¹ Legitimasjon, publisitet and notoritet. In my presentation i will use Appearance, publicity and evidence as an exact translation, despite his being somewhat unaccurate linguistic. However i believe it will ensure the most accurate presentation of norwegian law.

²² Lilleholt. (JV-1996-69 s. 70)(My translation)

²³ Lilleholt. (JV-1996-69 s. 70)(My translation)

²⁴ Lilleholt. (JV-1996-69 s. 70)(My translation)

²⁵ Lilleholt. S.169

dispositions that lesser the creditors right to cover must be controllable or verifiable in respect of the time of, but also content of the acquisition. Hence, the transaction must have evidence to not be extinguished by the creditors²⁶. This constitutes the core in the rules regarding creditor extinction.

That the transaction is public is not directly relevant in creditor extinction. However publicity regarding acquisitions may be relevant to a creditor with an unsecured claim. If the debtor starts selling or mortgaging his assets, or if other creditors claim disbursements, it may be a good indicator for the unsecured creditor to start recovering his claim. That this is a recognized consideration in property law²⁷ can be illustrated by the void in bankruptcy rule in the SCA act § 5-8. The creditor can claim bankruptcy proceedings with the debtor, and according to the SCA § 5-8 make any disbursements claimed later than three months before the filing date²⁸ have no effect towards the bankruptcy estate.

Appearance is not relevant in creditor extinction, as opposed to in extinction, which require good faith. Then the question of extinction is whether the acquirer B is in good faith, based on the outer reflection of right (appearance) of the disposer A. Still, the debtor's appearance is not completely without relevance in creditor extinction. The creditor can consider the debtor's outer reflection of being wealthy when granting unsecured credit. This can be illustrated by the fact that in all business in where the contractual object is delivered prior to payment, it is common to do a credit check on the buyer to consider his general financial situation. However, the creditor has no knowledge of to what extent the debtor is indebted to other creditors. As a consequence the debtor's credit appearance is not a considerable consideration in creditor extinction²⁹.

²⁶ Brækhus. S.499-517.

²⁷ Lilleholt. S.171

²⁸ The satisfaction of claims act. §1-2. The filing day in bankruptcy is the day when the pleading to file bankruptcy which was acted upon arrived at the court.

²⁹ Lilleholt. S.139-141.

An important element to consider when interpreting property law is the consideration of consequence and system in the rules³⁰. Property law are known to be particularly complex, as a consequence the system and consistency in the rules becomes a consideration in it self when interpreting legal materials³¹. In all areas of law consistency and system in the rules is important because it enables the public to predict their legal position. However it can be argued that it is particularly important in property law due to the particularly complex system of rules, and that it should be given additional weight when interpreting this area of law as opposed to others³².

1.7 Structure of the thesis

In chapter 2 I will present two of the most common standardized contracts: NSF 2000 and NF 05, in a creditor protection perspective. The aim is primarily to illustrate the problems that arise in these contracts in relation to bankruptcy or creditor seizures. The remaining part of the thesis will generally address the most interesting problems that arise in NSF 2000 and NF 05 more thoroughly. In chapter 3 I will present the rules for perfection through registration in the ship register/ship building register. To illustrate the special features of the rules in the MC I will compare them to the perfection rules for real property. In chapter 4 I will assess whether one can fall back on the perfection rules for chattels if the option to register the ship building contract/contractual object has not been used according to MC § 31. In chapter 5 I will present the perfection rules for chattels, and especially question whether there is an exemption from the handover requirement for manufacturing contracts, and if that is the case, the extent of this exemption.

³⁰ Lilleholt. JV-1996-69.

³¹ Lilleholt. JV-1996-69

³² Cf. Statements of the court in Rt.1998.268(Dorian Grey).Lilleholt. S.32.

2 Creditor protection in manufacturing contracts

2.1 Overview

In this chapter creditor security in NSF 2000 and NF 05 generally will be presented. To ensure the outlay in chapter 2 is as perspicuous as possible, I will presuppose that there is no exemption from the requirement of handover in manufacturing contracts. There is a lot of money involved when building a ship or an oil platform. This makes it important for the buyer involved to secure his interests against the yard's bankruptcy or creditor seizure. This can be done in many different ways. However in this presentation the security measures available to NSF 2000 and NF 05 will be focused. The reason I choose these two standard contracts, is that they are based on the two most common types of buyer's security. NSF 2000 is based on protection through bank guarantee. Bank guarantees secure the buyer's down payments, which is normally sufficient in ordinary ship building contracts. NF 05 on the other hand is based on the buyer registering as owner in the ship building register. Registration protects not only the buyer's down payments, but also the right to the contractual object itself. Hence, in case of the yard's bankruptcy, the buyer can move the contractual object to another yard to be finished. This is important because in the large building projects that NF 05 is meant for, one contract is usually only a small piece of a large puzzle. Specific performance is therefore of outmost importance³³.

The buyer finances the newbuilding through at least six³⁴ down payments³⁵. This is one of the typical features of manufacturing contracts. For each of the agreed down payments the buyer does not actually receive anything tangible in return. In other words, reciprocity in

³³ Kaasen.Petroleumskontrakter.Art.22

³⁴ NSF.1981.§4.

³⁵ Usually there are many down payments in fabrication contracts within the petroleum industry. Monthly payments are common. Knut Kaasen.Petroleumskontrakter.

the transaction is not fulfilled and the buyer is per definition granting the yard a loan³⁶. In this situation the starting point is that the buyer would be in the same position as any of the yard's other unsecured creditors in case of the yard's insolvency³⁷. As a consequence it is of the outmost importance for the buyer to secure his down payments, but also his interest according to the contract.

2.2 Creditor protection in NSF 2000

The main rule according to NSF art III is that the yard arranges a bank guarantee to secure the buyer's down payments according to the contract. Then the yard has the property in the newbuilding until delivery. In this arrangement the buyer's down payments are protected. However, the buyer has no separatist right to the ship it self, exceeding his contractual right to have the ship delivered according to the agreement. If the yard register their property in the contractual object, then this registration act also register the buyer's contractual right to the ship, cf MC § 31.1.

The question is whether the buyer is protected in the yard's bankruptcy if his contractual right in the ship is registered in the ship building register. (Contractual right, as opposed to property right)

Meland³⁸ refer to RG 2003.514 and argues that the buyer's right according to the contract is protected in such case. However, a right must either be a property right or a mortgage right to be protected in bankruptcy. The buyer's right according to the contract is neither a property right nor a mortgage right. Resulting in that it is not protected in the contracting party's bankruptcy, regardless of being registered. Registration of the buyer's contractual

³⁶ Reservation: The interest doctrine, and the exemption for manufacturing contracts. See Andenæs. Konkurs. Chap 19.

³⁷ The exemptions will be reviewed later in the thesis.

³⁸ Meland. S.175

right only protects him from the yard selling the ship to a third party outside bankruptcy³⁹. In RG 2003.514 the buyer was registered as owner of the newbuilding, this case is therefore irrelevant to this problem.

In order to have a separatist right in the ship in the yard's bankruptcy the buyer's right must be registered in the register of ships, (with the exemption of perfection according to the rules for chattes). According to NSF 2000 art. XI. "The buyer is entitled to let the contract and the ship under construction register according to the rules of the MC"⁴⁰. If the parties as an exemption have agreed that the buyer is the owner during the construction, he can register his property in the newbuilding. This is a condition to have a protected right to the ship itself in the yard's bankruptcy. This follows from the SCA § 2-2. As the ship is not property of the yard, it is not part of the yard's bankruptcy estate. It should be mentioned that the buyer also could secure his right to the ship by registering a security interest in the newbuilding. Cf. MC § 41 cf. § 42, § 43. Moreover a mortgage or any other charge on the ship according to MC § 41 also attach to the ship's separatist parts and appurtenances according to MC § 45⁴¹.

In the buyer's view it is obviously more desirable to have the property right in the newbuilding in addition to the bank guarantee. This especially the case in a rising market where the market price is likely to be higher on delivery, than when the contract was concluded. In case of the yard's bankruptcy the buyer could move the hull to be finished at another yard, thereby secure his surplus of the project. Moreover, from a commercial point of view it could be particularly important to have property right in the newbuilding in a rising market. The price the yard ends up paying for materials could be considerably higher than what was taken into account when the contract was concluded. The market for raw materials like steel is extremely volatile, and could vary considerably during the construction time, which could be several years. It is clear that a yard will include a certain

³⁹ Knutzon. S.33.

⁴⁰ My translation.

⁴¹ Bull.Falkanger.Brautaset. S.128.

margin when entering their bid, but due to heavy competition between the yards, this margin will be pushed to the limit in order to increase their chances of securing the contract. As a consequence the risk of bankruptcy in the yard is present also in a rising market. Hence, it becomes important for the buyer to secure not only his down payments, but also his positive contractual interest.

According to NSF 2000 XI the yard is entitled to mortgage the newbuilding and corresponding materials to secure the construction loan. This applies regardless who has the property right in the newbuilding. The mortgage will normally be on first priority⁴². Mortgaging of the newbuilding is regulated in MC § 41.3 and MC § 42. The scope of the mortgage right is regulated by MC § 43 and MC § 45. The security interest thereby also attach to the ship's separatist parts and appurtenances⁴³. If the buyer is registered as owner he must give his consent if the yard shall be able to encumber the newbuilding, cf. MC § 22. When the NSF standard formula is agreed, than this must be considered as consent to encumbrance. In that case the provision could constitute a risk to the buyer's financial security. Especially if the buyer lacks a bank guarantee to secure his down payments he is in a very unsecured position⁴⁴. The rule is a natural consequence of the security arrangement in NSF 2000, were the buyer is protected by a bank guarantee, while the yard has the property right in the newbuilding and thereby can encumber it.

If the buyer's right is not secured by a bank guarantee he should at least get a mortgage in the ship to an amount sufficient to secure his down payments with priority above the construction loan⁴⁵. However, when the buyer is not secured by a bank guarantee it is usually because he is registered as the owner of the newbuilding. As registered owner the buyer cannot register a mortgage bond for his own benefit. The mortgage default securing the construction loan is on the other hand a lien securing the claim of a third party.

⁴² Knutzon. S.33

⁴³ Bull. Falkanger. Brautaset S.128.

⁴⁴ Knutzon.Nordisk Medlemsblad.1984.nr.17.S.34

⁴⁵ Cf. MC §41.

Therefore the parties can agree that the lien securing the construction loan shall have priority after the buyer's right⁴⁶.

A specific problem arises if the hull is manufactured abroad. Then registration in the ship building register will not provide protection until the hull arrives in Norway, cf § 31. The hull under construction abroad will not be protected by registering the ship building contract in the Norwegian ship building register. This as in the ship building register there can only be registered ships that are under construction in Norway. In this situation the parties must register the hull under construction in the foreign register, and the mortgagee must accept registration of his lien in this register as sufficient security⁴⁷. The time period from the delivery of the hull in the foreign yard until the hull arrives in Norway constitutes another problem. The towage can last for several weeks. The hull must be deleted from the foreign ship building register before delivery can take place. Even though the building contract is registered in the Norwegian ship building register it is not decided in case law whether registered mortgages have perfection before the hull arrives in Norway. In this period one can depend on pledge lien constructions to obtain perfection.

2.3 Creditor protection in NF 05

The security arrangement according to NSF 2000 is somewhat different than the arrangement in NF 05 and NKT 05. According to NF 05 art 20.2 it is presumed that the company pays the supplier as the work progresses, and at the same time gains the property in the object of the contract. Cf. art 22.1. This provision is excessive, as the parties cannot agree upon conditions that weaken the position of third party creditors⁴⁸. It should be noted that this is parallel to the transfer of ownership if the company is registered as owner, cf MC § 31 cf. § 25. Hence, it could be practical to display the rule in the contract. However,

⁴⁶ Knutzon. S.34

⁴⁷ Meland. S.176.

⁴⁸ Lilleholt. S.198.

whether it display the mandatory legislation if the company is not registered as owner is not certain. This will be further discussed in detail in chapter 3.

According to art 22.3 the company is entitled to register as owner of the contractual object, the deliveries of the company, materials and the contract in the ship register. Further from art 22.2 it follows that the contractual object and materials the company have property right in shall be free from all encumbrances, except for any in which the company is liable. This rule is necessary in order for the company to have sufficient protection with only registered property right to the contractual object. This solution is different from the one in NSF 2000 XI. This is because NF and NKT have registration as the company's main security measure according to the contract while in NSF the buyer's right is protected by bank guarantee. When the supplier cannot encumber the contractual object during the building process he loses an important measure for financing the materials and the construction as it progresses. However this solution was chosen because NF and NKT are designed for projects where the yard is constructing only a part of a large puzzle. Then registration is just as important for securing specific performance⁴⁹ as for securing the down payments. Still, it is important to emphasize that art 22.2 only regulate the relationship between the company and the yard, and not the relationship to a third party which has right in the contractual object in conflict with this rule⁵⁰. If the third part right is an execution lien then the problem is regulated by MC § 31 cf. 23 (the same rule as in art 22.1). However, if the supplier voluntary has encumbered the contractual object or the materials in breach of art 22.2 then the problem are solved according to the rules regarding extinction in good faith, cf. The law of extinction in good faith § 1. According to art 21.1 the supplier is also obligated to supply a bank guarantee as security for his possible liability towards the company. In practice this usually constitutes between 5 % and 25 % of the purchase sum⁵¹. This arrangement is only meant as a supplement to the security provided through registration, primarily as protection from defects in the performance.

⁴⁹ Norsk: Naturaloppfyllelse.

⁵⁰ Kasen. S.542.

⁵¹ Kasen. S.525.

The purpose of the security measures in NSF and NF are very different. As mentioned, this is an expression of what it is important to protect in each standard contract. The specific performance in NF 05, opposed to primarily the down payments in NSF 2000. Further these are just standard contracts that the users usually change to a great extent in each individual agreement. This as one require different security based on who provides the financing, how the market is and who is actually purchasing the ship or offshore installation. Still, it is the same measures that are used individually or in combinations. The standard contracts are governed by mandatory background legislation. As a consequence the further discussion will focus on the presentation of these rules.

3 Creditor protection by way of registration

3.1 Introduction

3.1.1 Overview

The action, if any, which is required in order to protect a buyer of a right against later creditor seizures from the seller's creditors is referred to as an act of perfection. Perfection in relation to property rights can be obtained in three ways: registration in a register, by depriving the holder of actual possession and by notification⁵². In this chapter I will focus on registration. The rules regarding perfection by way of registration are found in the MC. I will not only present the rules, but also compare them to the rules in the Land Registration

⁵² In regard to security interests there are also other ways to obtain perfection. See the mortgage act. §3-17.

Act of 1935. Shipping is a unique international business, and I will examine how this may have affected the priority rules in the MC as opposed to the registration act. The registration rules are relevant in relation to the main problem of the thesis because the buyer have an option to register his property right according to MC § 31. When a professional buyer easily and effectively can secure his interest, then that constitutes a very important factor in determining whether he should be protected if the registration option has not been used. Further, the presentation of the registration rules shall illustrate how the legislator has used consistency and system in the rules as a factor in property law. This is relevant to determine how system and consistency can be used as a factor when assessing whether the perfection rules for chattels can be applied if the registration option in MC § 31 has not been used, which is the main problem of the thesis.

3.1.2 The different types of legal registers

There are several classes of registers regarding rights in assets. The difference between the classes of registers, depend on to what extent the register provide legal protection. The most important kind is property registers⁵³. According to the mortgage act § 1-1.4, a property register is register of rights which ownership and in principle all encumbrances in register able assets can be registered. It is “arranged according to the assets in which rights are concerned”. To register a right in a property register will protect the right in question against non-registered third party rights, and registered rights registered later than the initial right. This applies regardless of the kind of right and regardless the type of the third party, with the exemption of rights arising directly from enactments. Examples of property registers are: The Real Property Register⁵⁴, the Ship Register and the Aircraft Register.

There are also other legal registers. This is an aggregate group of registers that provide perfection in some but not in all third party conflicts. An example is the Patents Register. It

⁵³ In Norwegian: real register cf. Mortgage act § 1-1.4.

⁵⁴ Grunnboken

provides perfection only in relation to credit seizures and double conveyance conflicts. Another example is the Chattels Register, which is a register for security interests in chattels. By registering a security interest in the chattels register the holder of the security interest is protected from other security interests that is not registered, or registered after it. However the holder is not protected from a sale of the asset itself or a pledge based on possession, cf The Mortgage Act § 3-1, cf § 3-2. (There is one exemption⁵⁵). This is a consequence of the fact that the Chattels Register as opposed to property registers, do not provide conclusive evidence of the rights in the asset, and perfection for chattels can only be obtained through possession⁵⁶.

3.1.3 Justification of registration of rights in property registers

Registration of an older right in a property register will always provide protection against a younger creditor seizure, as well as against any other third party right that is registered later than the original right, (with the exemption of MC § 25). In the light of the evidence and publicity provided through registration this is a very nearby solution. The registration makes both the time of occurrence of the right, and to some extent the content of it, verifiable. Hence, registration provides evidence in relation to the transaction. Through evidence regarding the transaction, the registration rules effectively remedies creditor fraud, which is the main consideration behind rules allowing a creditor to extinguish another successor's right in an asset. However, it should be mentioned that to avoid creditor fraud the registration rules are also supplemented by the avoidance rules in the Satisfaction of claims act⁵⁷.

Although registration in a legal register gives the owner of a right extensive protection, the rules have weaknesses. Firstly, it does not matter if a transaction certainly can be verified, if it is not registered, then the other right will be extinguished. For example an old right to

⁵⁵ The exemption is motor vehicles RTA§ 15 Cf. §16. The mortgage act. §5-5. Moreover, §§ 3-8 and 3-17

⁵⁶ Lilleholt. (JV-1996-69 s.84)

⁵⁷ SCA. Chap.5 (Spes.§5-8)

use a property will be extinguished if it is not registered, regardless of whether the contractual basis can be documented, as well as continuous usage. However, this is to a certain degree remedied by the fact that some statements in theory and case law assume it is possible to obtain acquisitive prescription⁵⁸ of perfection⁵⁹. The core of their reasoning is that a rightful owner should not be situated worse than someone who is not owner but gains ownership through acquisitive prescription. However, there is opposition among scholars⁶⁰ against the registration act § 21.2 being interpreted this extensively. This is also supported by case law in Rt.1996.918. Hence it is not possible to obtain perfection through acquisitive prescription.

Secondly there is a weakness that one always run the of risk human or technical failures in the registration system. If there are failures in the registration system, one risks suffering extensive losses. Since one is relying on external sources in determining whether there are any encumbrances to an asset there is always a risk of failures that weakens the appearance and evidence of the register. This is however to a certain extent remedied by the MC § 37. According to this paragraph, A is entitled to compensation from the government if he has suffered a loss due to a registration error and is without blame. There is a parallel rule regarding real property in the land registration act. § 35. In order to present a more thorough analysis on registration of rights in property registers, one must assess the substantive rules. In the further presentation I will briefly present the Norwegian ship registers, and thoroughly present the rules for establishment of perfection.

3.2 The ship registers (NOR/NIS)

3.2.1 Overview

⁵⁸ Hevd.

⁵⁹ Rt.1995.205.Brækhus. S.571.

⁶⁰ Marthiniussen. (JV-2003-264)

A ship is identified by the flag it fly's. Which flag they fly depend on in what country's ship register they are registered. In Norway we have two different ship registers. The Norwegian ship register (NOR), and the Norwegian international ship register (NIS). Registration of a ship has both private and public aims. The first is to ensure that the owner of the ship is properly identified so that official directives and possible enforcement actions can be addressed to the right party. The other is to work as a register for legal rights in the ship. The registers are separatistd in the way that they have different legal basis. NOR has its basis in the maritime code, and NIS in the NIS act. In the last 20 years the legislator has harmonized these rules so that they are nearly identical⁶¹. As a consequence I will focus my discussion on the presentation in the maritime code.

Norway has traditionally been a country that has imposed strict conditions for registration in the ships register, and at the same time requiring ships satisfying those conditions to be registered in the Norwegian register. However this has to a large degree been changed. The two ship registers have different conditions for registrations. As this presentation will focus on the property law problems in manufacturing contracts, I will not go into the specific conditions for registration in NIS/NOR.

3.2.2 The ship building register

The ship building register is a sub-section of the Norwegian ship register. According to MC § 31 ships under construction can be registered on request of the owner and ship building contracts can on request of the buyer be registered in the ship building register. The only prerequisite is that the ship will be more than 10 meters long⁶². When a contract is registered this registration will also include the buyer's contractual right to the newbuilding⁶³. According to MC § 31.3 the rules regarding registration of rights in ships

⁶¹ Thor Falkanger, Hans Jacob Bull Lasse Brautaset. Scandinavian maritime law. The Norwegian perspective. Second edition. 2004. Chap. 2. S. 63.

⁶² MC. § 31.

⁶³ Knutzon. Nordisk Medlemsblad. 1984. nr 17. S. 34

applies correspondingly to registered ships under construction and registered ship building contracts. The same applies for the assets that can or shall be registered in the ship register that are not considered to be ships. See 2.3.3.5. The rules regarding registration of ships in chapter 2 in the MC apply correspondingly to registered ships under constructions and ship building contracts as far as they are fit, cf. MC § 31.3⁶⁴.

The characteristic that makes the ship building register unique in comparison with other legal registers is that registration is voluntary. This complicates the legal regulation of a ship under construction. The legal basis when the contract or newbuilding has not been registered will be extensively discussed in chapter 3.

3.3 Perfection

3.3.1 Introduction

The rules regarding perfection in relation to rights in ships are to a large extent equal to the rules regarding perfection of rights in real property. However there are important differences. Especially due to the international characteristics of shipping a more advanced system of registration was required⁶⁵. As a consequence it is recognized that there are significant differences between the rules regarding registration in real property and ships. One can always question the system and consistency in the rules when two parallel registers are regulated by different rules. In this chapter I will present the priority rules in the maritime code and especially question the rules that differ from the rules in the registration act.

⁶⁴ MC§313.Sub-section.The rules in§11.4,§12.2,§13,§14.1-4,and §§15-27 applies correspondingly as long as they fitt.

⁶⁵ Opinion.Thor Falkanger.

The relevant problem is whether the differences in the MC and the registration act can be justified by the special features of international shipping

3.3.2 What can be registered

According to MC § 20 “In the ship register it can be registered documents that is to establish, alter, transfer, encumber, confirm or revoke a right in a registered ship”⁶⁶. This implies that registration of rights may take place to the same extent as the recording of rights in real property. Deeds, purchase contracts, purchase options, mortgages and negative pledge agreements can be registered. However there are two exemptions according to § 20.2 sentence. Documents regarding leasing or chartering of a vessel, so-called charter parties cannot be registered. The rationale behind this is that it would have been impossible to obtain court decision for the specific performance of the charter party. Further it is considered to be an undesirable situation that a ship would be forced to perform a charter party under the threat of a daily fine. For a straight bareboat charter party the concerns are somewhat different, but it would be difficult to distinguish some bareboat and time charter parties, the exemptions therefore also covers bareboat charter agreements⁶⁷.

The second exemption is that maritime liens in a ship cannot be registered. A maritime lien is a statutory lien that is automatically created to secure certain claims related to the ship, in the ship itself, cf. MC § 51. The argument for denying maritime liens to be registered with a ship in the ship register is that the register would not provide conclusive information about the maritime liens claims. To illustrate; if there has been a collision, have any maritime lien claims arisen? If that is the case, then how many, and to what amounts?⁶⁸

⁶⁶ My translation

⁶⁷ Thor Falkanger, Hans Jacob Bull Lasse Brautaset.Scandinavian maritime law.S.65.

⁶⁸ Falkanger, Bull, Brautaset.S.65

3.3.3 The material perfection rules

3.3.3.1 Overview

Perfection is established by registration of the right in question in the ship register. The statutory authority follows from MC § 20. “In the ship register it can be registered... right(s) in a registered ship”. However MC § 20 must be viewed in the light of the priority rules in MC §§ 23-25. The rules regarding perfection of rights in ships are as mentioned to a large extent parallel to the rules regarding perfection of rights in real estate in the Norwegian Registration Act. The relevant problem regarding establishment of legal perfection is; when must registration have taken place at the latest in order to be protected. This depends on the nature of the contending right.

3.3.3.2 The contending right is an execution lien.

The main rule regarding perfection in relation to credit seizures in a ship follows from MC § 23. According to the first sub-section “registered rights pass non registered rights” and according to the second “if several rights collide then the first right to be registered in the property register will prevail”. It is the exact time of the registration that is decisive for which right that prevails. This differs from the rules regarding real property, where an acquisition by way of contract must be registered the day before the contending execution lien to prevail⁶⁹. Before 1992 the rules in the Maritime Code were parallel to the rules in the registration act on this point. However they were changed to ensure legal unity with the NIS register when the NOR and NIS was restructured in 1992^{70, 71}. When the NIS register was established in 1987 the lawmaker wanted the exact time to be decisive for perfection in relation to execution liens. The rationale behind this is that there is no reason an owner of

⁶⁹ The Norwegian registration act §20

⁷⁰ Op.prp. Nr. 41 (1991-1992).

⁷¹ FOR.1987-06-26 nr.554 §20. OPPHEVET.

an execution lien should be in a better situation than an acquirer by way of contract. However, consistency and system in the rules are especially important in property law.⁷² Therefore it can be a basis for criticism if the lawmaker deviates from the system, without proper reasoning. However, the system of the maritime code is more advanced, and the solution of priority by time is easier to implement in the MC than for the extensive group of rights in the real property register, therefore this solution was chosen. Further the requirement of an advanced system with time priority regarding the registration of rights was a necessity in order to provide a competitive registration for international tonnage.

The third sub-section specifies the priority system further as the “rights that are registered at the same time are equal”, but that “execution liens surpasses acquisitions by way of contract” and if “several execution liens are registered at the same time the oldest will prevail”.

3.3.3.3 The contending right is a bankruptcy or a “compulsory composition”⁷³.

Regarding bankruptcy or compulsory composition registration is only required to protect a voluntary acquisitioned right. The right in question must be registered the day before bankruptcy is opened⁷⁴. This rule is equal to the one in real property. Hence “Voluntary acquisitioned right” must be interpreted equally as “right by way of contract” in the registration act § 23⁷⁵. What is required for an execution lien to be protected in the debtor’s bankruptcy is not regulated in the MC, nor in the in the registration act regarding real property. Here the rules of registration must be viewed in the light of the avoidance rules in the SCA. According to the SCA § 5-8 cf. § 5-10⁷⁶ an execution lien registered with the

⁷² Rt.1998.286 (Dorian Grey)

⁷³ Tvangsakkord is a composition of creditors where minority of the creditors have been forced into debt arrangement by the majority of creditors. Cf. The Bankruptcy act chap.6.

⁷⁴ SCA § 1-4.3. The opening of the bankruptcy is when the order to open bankruptcy proceedings is granted.

⁷⁵ Andenæs. S.187.Cf. Rt.1998.268.

⁷⁶ Satisfaction of claims act.§5-10. In this chapter a disposition is not considered performed until it is perfected.

debtor later than three months before the filing date⁷⁷ has no legal effect towards the bankruptcy estate. In reality, this is not a perfection rule, but a rule regarding distribution in the bankruptcy. If a creditor gets an execution lien registered close to the bankruptcy, there is usually no reason for him to prevail over the rest of the bankruptcy estate.⁷⁸ Without SCA § 5-8 the debtor's creditors would be forced to follow an initial creditor seizure to secure their interest if they know the debtor could be close to bankruptcy. This would lead to more bankruptcies, and unfortunate random distribution in the bankruptcy estate.

SCA § 5-8 is in reality a void in bankruptcy rule as opposed to a perfection rule. This can be illustrated by that a younger right by way of contract is protected from the estate, but must respect a younger execution lien. The right by way of contract is registered before the opening of the bankruptcy, but after the registration of the lien. If § 5-8 were a perfection rule, this would be a so-called impossible priority conflict. Where one would consider the considerations behind the perfection rules to decide which right should prevail. But in this case the void in bankruptcy of the execution lien is in the benefit of the bankruptcy estate, not for the benefit of the contractual right. Hence, the holder of the execution lien will prevail. This understanding is based on the argumentation in RG 1987.312⁷⁹.

3.3.3.4 Exemptions from the priority rules

Exemptions from the priority rules are regulated in MC § 24. These rules apply equally if the contending right is an execution lien, a bankruptcy or a compulsory composition. The first sub-section is only relevant for extinction in good faith, and hence not for creditor extinction. The second sub-section states that rights based on statutory authority, do not have to be registered to have perfection in relation to third party rights. This rule must be seen as an expression of statutory rights having absolute evidence, and to some extent publicity.

⁷⁷ Norwegian: Fristdagen. The filing date of the bankruptcy is the day when the request for opening of bankruptcy, that was acted upon, arrived at the court.

⁷⁸ Lilleholt. S.181.

⁷⁹ Lilleholt. S.181.

Further the consideration to avoid creditor fraud does not apply in relation to statutory rights.

According to § 24.3 there is an exemption from the priority rules regarding reservations in the contractual object at the time of the transfer. For instance may the seller have made a reservation of the property right in the asset to secure the remainder of the purchase sum⁸⁰. Such reservation will prevail in relation to rights excreted by the new owner, as long as the reservation is stated in the buyer's bill of sale, or is registered no later than the bill of sale. If the buyer's creditors have acquired an execution lien in the ship, and registered it on 1st August, then the seller's reservation in the bill of sale, which is registered 1st September, will prevail. If there are several rights derived from the seller the relationship between them are regulated in § 23. This rule corresponds to the rule regarding real estate in the registration act⁸¹.

Further there is a rule regarding the entity financing the ship. If the financier acquires a security interest to secure his credit performance, and it is registered the same day as the document of authority at the latest, it is protected from previously registered execution liens from the new owner's creditors. The rationale behind this rule is that the entity financing the purchase of the ship must have a fully secured mortgage without having to rely on the full co-operation of the seller. Without this rule the financier is not even secured if his mortgage is registered simultaneously with the transfer of ownership. He risks getting priority behind an execution lien entered at the same time, or if the seller reaches bankruptcy the same day. This rule is an expression of the utmost importance of the mortgage in ship purchase contracts. Especially due to the development towards arranging ship owning companies in several one-ship-companies it is important to protect the financier from a seller's unexpected bankruptcy. Moreover this rule is supported by the consideration of making the register competitive in international shipping. It would not be very desirable for banks to finance the purchase of ships registered in NIS/NOR if their

⁸⁰ In that case the reservation must be created according to the rules of the mortgage act.

⁸¹ The Norwegian registration act. §21.3.1.Sentence.

mortgage was not sufficiently secured, and particularly if other registers could provide such security.

In relation to real property there is a similar rule regarding security of financing a purchase in a forced sale⁸². However there is no equivalent rule applicable to an ordinary sale of real property. Viewed in light of the day- priority rule in the registration act § 20 this is somewhat strange, as the financier is positioned even weaker than in the main rule of the MC. Considering that the financiers in a real property sale have the same uncertainty ensuring their mortgage lien as the financier of a ship, one could think that there should be an equal rule in the registration act. This would improve the financier's position in securing his mortgage, and improve the financial safety in real property transactions. Further, it would improve the consistency and system in the property rules, as there would be parallel rules for ships and real property. When such a rule does not exist regarding real property, it is probably rather due to the special features of international shipping that make the rule necessary in relation to ships. The risk of bankruptcy is not as pressing without one-ship companies, and the extensive liability a ship owner may be exposed to. Also the land register has no competition from other legal registers. As a consequence it is possible that the lawmaker is more reticent in making rules that protect against a somewhat theoretical risk.

According to § 24.4 the rules in MC § 24.3 applies equally when a ship is initially registered. Regarding delivery from a foreign yard or a foreign seller, registration can take place prior to delivery, cf. MC § 14.5. Then registered rights in the ship are considered registered at the time and day of the delivery. Further, according to § 24.4 rights transferred from a foreign register according to the MC § 74, have priority above all other encumbrances, with internal priority according to the registration in the foreign register.

According to § 24.5 the registration rules do not apply in relation to transfer of a lien, or a pledge of a lien tied to a negotiable promissory note according to the promissory notes act

⁸² The Registration Act. §21.3.Sub-section.2.Sentence.Cf: Norwegian enforcement act. §11-33.2

§ 11.2. Then priority and perfection are regulated by the rules regarding claims and the mortgage act's rules regarding pledges in securities⁸³.⁸⁴ This rule has a parallel rule in real property⁸⁵. In retrospect it should be explicitly mentioned that an execution lien in a maritime lien must be registered to have protection.

3.3.3.5 Perfection in ships under construction, ship building contracts and other structures that can or shall be registered in the ship register

The rules regarding registration of ships in chapter 2 in the MC apply correspondingly to registered ships under constructions and ship building contracts as far as they are fit, cf. MC § 31.3⁸⁶. The same applies for the other structures that can or shall be registered in the ship register. This also applies for structures that cannot be considered ships according to MC § 33⁸⁷, solid structures under construction for exploration or exploitation of natural resources according to MC § 39, and drilling platforms or other similar floating structures according to § 507⁸⁸. The situation when a ship under construction, a ship-building contract or other contract can be registered, but the opportunity has not been used is not regulated in the maritime code. However I will thoroughly go into the state of law in this situation in chapter 3 of the thesis.

⁸³ The Mortgage Act. §3-2.

⁸⁴ Gyldeendal rettsdata. MC §24.5

⁸⁵ Registration act. §22.

⁸⁶ MC§313.Sub-section.The rules in§11.4, §12.2, §13,§14.1-4,and §§15-27 applies correspondingly as long as they fit.

⁸⁷ MC§31.3.The rules in§11.4+5, §12.2, §§13-30 applies correspondingly as long as they are fitting. Regarding structures mentioned in 1.MC §31.1+3, and §32 also applies correspondingly.

⁸⁸ MC. §507.2.Sub-section. The structures are considered to be ships, hence the rules in MC.Chap.2,3,4,5,6,7,8,9,16,18,19,20 applies correspondingly. (With mentioned exemptions).

4 Perfection if the contract/contractual object is not registered

4.1 Introduction

This chapter constitutes a part of the main problem of the thesis. According to MC § 31 it is voluntary to register a ship building contract or a newbuilding. As long as the option to register has been used the priority rules of the MC apply equally as for operational ship registered in NOR/NIS⁸⁹.

The question is however whether the buyer must use the registration option in order to have a protected right in the newbuilding or whether they can apply the perfection rules for chattels.

The problem is not regulated in the MC, and only sparsely covered by case law. The starting point in this discussion must be taken in case law, and to compare this with the legal theory. The definition of chattels is all objects that are not real property. Ships or platforms under construction are thereby per definition chattels⁹⁰. So if the registration option has not been used it is a nearby solution to apply the perfection rules for chattels. To apply the perfection rules for chattels was also the solution chosen in the only decision so far on this matter, the Bomek-case⁹¹. The decision was appealed, but the dispute was resolved by way of a settlement before there was a new decision. The courts solution has wide support in legal theory⁹². If it is possible to apply the perfection rules for chattels, then registration is not a necessary condition for the buyer's property right in the contractual

⁸⁹ Meland. S.175

⁹⁰ Ships or platforms under construction are register able chattels, cf § the mortgage act. §3-3, cf. MC §22 cf. §31, Cf §507.

⁹¹ ND.1982.264 (Bodø Namsrett) The court applied the interest doctrine and redjected that the buyer had a separatist right to the moduel.

⁹² Selvig ND.1982.s.X111,Kruger. S.136-137.Lilleholt. S.199.

object. It should be emphasized; it is only the court's solution to apply the perfection rules for chattels that has wide support in theory, not the entire decision.

In the following I will question whether the nature of the property right in the contractual object impose restrictions on the applicability of the perfection rules for chattels, and generally discuss whether the chattels rules can be applied if the contractual object is not registered.

4.2 Whether the perfection rules for chattels is applicable if the contract is not registered

4.2.1 Introduction

This problem can be approached from several angles. The consensus in theory is that one should generally question whether it is possible to apply the perfection rules for chattels if the contract/newbuilding is not registered. Then the discussion should be based on the statements of the court in the Bomek-case and the theoretical presentations of Falkanger, Kaasen and Andenæs⁹³. Another angle that has not been discussed in legal theory previously is whether the buyer's property right in the contractual object is a security interest. This would give the result of the mortgage act being applicable. According to MC § 41 a security interest in a ship/ship building contract must be registered in the ship register to obtain perfection. Applied on the buyer's property right in the contractual object; the buyer must register his property right or security interest in the contractual object to be protected in the yard's bankruptcy. The result may be that one cannot apply the perfection rules for chattels if the buyer is not the registered owner or mortgagee. In my presentation I will start by discussing whether the buyer's right in the newbuilding is a security interest.

⁹³ Kaaasen. S.539.Andenæs. S.185.Falkanger. S.626.

Secondly, I will discuss the general angle in line with legal theory. In this discussion I presume that there is an exemption from the handover requirement for chattels to obtain perfection in manufacturing contracts. The question of whether there actually exists such exemption is discussed thoroughly in chapter 5.4.

4.2.2 Is the buyer's non-registered right in the contractual object in reality a security interest?

The buyer's property right in the contractual object during the construction is an arrangement with no other purpose than to give the buyer security for performance of contract, parallel to his down payments. As a consequence one can argue that the purchasers need for such security must be assessed equally as a security interest, resulting in MC § 41 being applicable. The political justification for legalizing the contractual security interest is that it creates credit⁹⁴. However as security interests directly displace the debtor's other unsecured creditors it is clear that the possibility to create security interests should be limited⁹⁵. This is achieved through the rules of the mortgage act, which is mandatory in relation to all security interests. As a consequence, it is of outmost importance to determine whether the buyer's right in the contractual object during construction is a mere circumvention of the rules of the mortgage act.

According to MC § 41 a security interest by way of contract can only obtain perfection through registration in the ship register. In other words, if the buyer's right to the contractual object during construction is a security interest, there could be no exemption from the requirement of handover in manufacturing contracts, that can be registered in the ship building register according to MC § 31. The starting point in this discussion should be the mortgage act § 1-1.1. "A security interest is a privilege to take cover for a claim, in one or more specific assets.

⁹⁴ Skoghøy. S.26

⁹⁵ Skoghøy. S.27

The question is whether the buyer's right in the contractual object during construction is a privilege to take cover for a claim.

The main consideration against considering the buyer's right in the contractual object a security interest is that it has no support in legal theory, or any other valid legal source. This indicates that the buyer's right is not a security interest.

However, there is neither any legal source that explicitly excludes this interpretation. The main consideration for that the buyer's right in the contractual object during construction is a security interest is that the purpose is to give the buyer security for his claim for specific performance. To give the buyer security for his claim is the same purpose, as a security interest according to MC § 41. This indicates that to consider the buyer to be owner during construction would be a circumvention of MC § 41.

The wording "privilege to take cover for a claim... in a specific asset"⁹⁶ indicates that the holder of the interest is entitled to have his secured claim covered prior to the debtor's other creditors, in reality, by a direct right in the specific asset in question. It is the privilege to take cover which recognizes the security interest, and which gives the security interest its value⁹⁷. The theory of the buyer's right in the contractual object under construction is based on the buyer becoming owner of the contractual object as soon as the construction starts, without any outer verifiable action. The core of the discussion is whether the right that the buyer gets in the contractual object can be verified to be a property right, or merely a privilege to cover a claim.

The buyer's right in the contractual object must be viewed in light of the definition of property in Norwegian law⁹⁸. Property right is negatively limited, which mean that it is

⁹⁶ Mortgage Act. §1-1.1.

⁹⁷ Skoghøy. S.23.

⁹⁸ Cf.1.4.

limited by other parties' positive limited rights in the asset. If the buyer's right shall be considered a security interest it should not give the buyer any other right of disposition than to take cover in the object to secure his claim.

It is clear that the buyer can sell the contractual object under construction. This is however an expression of the buyer's contractual right to the newbuilding during construction, and is thereby not related to his perfected protected right in it. Beyond his right of disposition in relation to his contractual right in the newbuilding, the buyer has no actual right of disposition⁹⁹. Resulting in that the buyer's right of disposition is limited to what it would have been if it had been a security interest according to MC § 41. This indicates that to consider the buyer's right in the asset during construction a property right would be a circumvention of MC § 41.

According to the contract, the buyer has a claim from the yard for specific performance. Usually the secured claim is a claim for money, but there is no problem that the claim being secured principally is for specific performance¹⁰⁰. There is in other words no problem in having a security interest protecting the specific performance of building a ship or a module for an oil platform. It should be mentioned that in reality, it would be the economic interest of the specific performance that is secured¹⁰¹.

Considering the buyer's right to the contractual object during construction a security interest would ensure predictability through systematic and clear-cut rules in property law. This as an exemption from the requirement of handover for manufacturing contracts would effectively be blocked. If the buyer must register his right to the contractual object, either through a security interest¹⁰² or by registering as owner¹⁰³, to be protected, the legal position of both buyer and yard become more predictable. This would ensure a simpler and

⁹⁹ Cf.1.4.

¹⁰⁰ Skoghøy. S.24.

¹⁰¹ Skoghøy. S.24.

¹⁰² MC §41.Cf. §31

¹⁰³ MC §20.cf. §20.

more international competitive legal framework. The buyer's non-registered right to a contractual object that can be registered, during construction, should therefore be a security interest according to the mortgage act § 1-1 1, cf. MC § 41. The result is that the perfection rules for chattels cannot be applied if the buyer is not the registered owner or mortgagee.

In the rest of the thesis it is presumed that the buyer's right to the contractual object is not a security interest.

4.2.3 Generally, whether the perfection rules for chattels is applicable in the situation where registration option has not been used

4.2.3.1 The state of the law

Based on a more general assessment, I will discuss whether the perfection rules for chattels are applicable, where the option to register a contract/newbuilding according to MC § 31 has not been used. The main argument against that the buyer must be the registered owner to be protected, is that he has an option to register, and when he has not used this option he should not be protected. This argument is strengthened by the professionalism of the parties in these projects. It is hard to imagine a professional buyer not securing his right according to the contract against the other party's bankruptcy.

Another important consideration against applying the perfection rules for chattels, if the registration option has not been used is the close relation between transfer of ownership and pledging. The pledge rule is in many ways parallel to the perfection rules for chattels. Therefore it can be argued that since register able chattels cannot be pledged, it should neither be possible to obtain perfection for register able chattels by applying the perfection rules for chattels. It is logical that the pledge rules and the transfer of ownership rules should be parallel since they revolve around the same asset, with the same perfection

action¹⁰⁴. If these rules were different, we would risk a pledge being camouflaged as an actual transaction, or the other way around¹⁰⁵. Further, if the buyer can have property right in the newbuilding without registration it should be questioned how any mortgages in the newbuilding could obtain perfection. The mortgage act § 3-2 explicitly prohibits a pledge lien to be founded in real registerable chattels, and if the building contract is not registered then it is not possible to register a mortgage in the newbuilding either. A pledge lien can be founded in chattels that cannot be registered in a property register¹⁰⁶, cf. the Mortgage Act § 3-2¹⁰⁷. If it can be registered in a property register it must be encumbered according to the mortgage act § 3-3¹⁰⁸. Hence, if the buyer can have property right to the newbuilding without registration then this would lead to an unsatisfactory arrangement regarding the possibility to encumber the newbuilding¹⁰⁹. This indicates that one should not be able to apply the chattels rules where the contract/newbuilding have not been registered.

The main argument for applying the perfection rules for chattels if the registration option has not been used; is that the considerations behind a modified handover requirement in manufacturing contracts should not be affected by the establishment of a rule with an option to register¹¹⁰. To apply the perfection rules for chattels in manufacturing contracts have an extensive foundation in Norwegian law, through the presentation of Brækhus Herrem, and the support it has gained. This indicates that the lawmaker should be relatively clear if the intent was to change the perfection rules. There is nothing in the preparatory works suggesting that the intention was to change the perfection rules. On the contrary the Maritime Law Commission explicitly tried to improve financial security through allowing ships under construction to be registered. Their intention was not to change the relationship

¹⁰⁴ Lilleholt. S.192-193.

¹⁰⁵ Lilleholt. S.193.

¹⁰⁶ The mortgage act. §3-2(Realregister).

¹⁰⁷ Ot.Prp.1980.S.110.

¹⁰⁸ Rg.1993.565 (Ofoten).

¹⁰⁹ Enforcement liens can be registered in the Chattels Register, cf. §41.3.

¹¹⁰ Kaasen. S.535.

between the buyer and the yard's bankruptcy¹¹¹. This indicates that if the registration option has not been used, the perfection rules for chattels should be applied.

The state of the law presented in theory is somewhat uncertain. Kaasen argues that the question is not solved but that strong considerations support that the buyer's property right should be protected if the contract is not registered¹¹². According to Falkanger, if the contract is not registered, then the perfection rules for chattels apply¹¹³. This is also supported by Andenæs¹¹⁴. It must be decisive that the only decision on the matter states that the chattels rules apply if the contract is not registered, and that this is followed up in theory.

4.2.3.2 De lege ferenda

Another affair is how the law should be. Mortgaging the newbuilding is an essential piece in financing the actual construction process. Therefore it is an unsatisfactory situation if the newbuilding cannot be mortgaged during construction. Furthermore, such a rule would weaken the consistency and system in the legal system. Property law consists of an especially complex system of rules, which makes consistency and system in the rules necessary for the public to be able to predict their legal position¹¹⁵. Firstly, this is relevant if the buyer has no right to the newbuilding unless he is the registered owner, this would make the ship building rules parallel to the rules of real property and ocean-going ships, as well as the pledge rule in the mortgage act § 3-2. Secondly, this would be a far clearer cut rule regarding the ownership of the newbuilding. As there is also uncertainty whether and if to what extent there is an exemption from the handover requirement for chattels regarding

¹¹¹ Kaaasen. S.537.Selvig. ND.1982.S.XIII with references to the preparatory works of MC.

¹¹² Kaaasen. S.539.

¹¹³ Falkanger. S.626.

¹¹⁴ Andenæs. S.188.

¹¹⁵ Rt.1998.268. (Dorian Grey)

manufacturing contracts it would be process economically to have a clear cut rule where one did not have to assess the rules for chattels, as well as the registration rules. Moreover the parties to these contracts are usually professional players, and as a consequence it would be reasonable to leave them without a separatist right to the newbuilding, if their property right has not been registered. In the light of these considerations I think that it would be better if the buyer had no right to the newbuilding in the yard's bankruptcy if he is not registered as owner or has a registered security interest.

5 Creditor protection regarding chattels

5.1 Introduction

5.1.1 Security for the buyers claim – Legal protection by agreement or handover?

In this chapter I presuppose that the perfection rules for chattels are applicable if the option to register the newbuilding/contract according to MC § 31, have not been used¹¹⁶. The presentation will include all the rules relating to perfection of rights in chattels. By presenting all the rules I will be able to assess which factors are relevant to the discussion of whether there is an exemption from the requirement of handover for manufacturing contracts.

¹¹⁶ Cf: Chap 4. Andenæs. S.187.

Chattels are “exterior tangible assets which is not real property, with the exemption of securities, registered ships etc. planes, and parts of or accessories for real property, ships and planes”¹¹⁷. The perfection rules for chattels are based on non-statutory law.

The question is whether the acquirer of chattels is protected against the disposer’s creditors.

This is a classic problem in property law and scholars have discussed the problem for many years. Therefore, to understand the present state of law of the perfection rules for chattels, the theories presented in the past must be assessed. This is because the current state of the law is based on these theories. The applicable law has usually been modifications of two major theories: The agreement principle and the traditional principle. In the agreement principle the acquirer is protected from the disposer’s creditors as soon as the contract is binding. While in the traditional principle the object of the contract must be handed over, or at least removed from the disposer for the acquirer to be protected¹¹⁸. Central in this discussion was the transfer of ownership’s close connection to pledges. When handover became a requirement to obtain perfection in chattels in 1857¹¹⁹ this heavily influenced the discussion of what it takes to obtain perfection in a sale¹²⁰. I will discuss the transfer of ownerships close relation to pledges in 5.3.3.

What is considered to be the state of law in Norway has changed several times. But, today the law must be defined as a “modified requirement of handover”¹²¹. I will start by presenting the main condition for handover, and then assess the modifications.

¹¹⁷ Def. Lilleholt. S. 188. (My translation).

¹¹⁸ Lilleholt. S. 189.

¹¹⁹ The Mortgage Act of 1857 § 1.

¹²⁰ Falkanger. S. 621-622.

¹²¹ Brækhus. S.499-517.

5.2 Perfection regarding chattels

5.2.1 The main rule

The main rule relating to perfection of rights in chattels is that the chattel must be handed over to the acquirer, or more precise the disposer must have lost the physical control over it for the acquirer to obtain perfection for the transaction¹²². If the acquirer already holds the contractual object, then perfection is obtained when the contract becomes binding¹²³. Equal to handover is a message of the transaction to a third party that holds the contractual object.

5.2.2 The core of the problem

The core of the problem regarding perfection for chattels are when the acquirer partially or fully has paid for the contractual object, but the seller still has the possession. If the acquirer must accept the seizure, he still has a claim for repayment of the purchase sum. But this is usually of little help if the seller is in such a financial situation that creditors seize his assets. It should be mentioned that the creditors could claim the debtor bankrupt if he is insolvent, cf. the bankruptcy act § 60. But then he will only get the dividend of his claim, cf. coverage act. § 9-6.

5.3 Perfection without handover

5.3.1 General regarding perfection, with basis in case law

¹²² Lilleholt. S. 190. Falkanger. S.621.

¹²³ Falkanger. S.621.

The question is in what situations removal of possession or the like is not required for perfection.

There is little case law on this subject. The most relevant cases are Rt.1910.231 “The cow-case” and Rt.1912.263 “The iron scrap-case”. These cases constituted the core in Brækhus’ and Herrem’s thorough presentation of the perfection rules for chattels¹²⁴, which has gained support both by scholars¹²⁵, and the courts¹²⁶. In the cow-case¹²⁷ eleven cows were sold for slaughter. According to the contract the seller was supposed to have the cows as long as they could produce milk, and the buyer was to pay when the transfer was concluded. When the seller went bankrupt only one of the cows were delivered. The court decided that the buyer did not have perfection in relation to the ten cows still located at the sellers, because there had been on real transaction of property.

In the iron scrap-case¹²⁸ it had been concluded an agreement for the purchase of all waste iron a shipyard would produce in 1908. The agreement was concluded in March 1908. The iron scrap was as agreed stored on the property of the yard, (the seller). Some of it was picked up in October, but when the yard went bankrupt in January 1909, there were still about 100 tons left. The purchaser had paid for 94 tons, and requested that it would lie at the yard until February. The majority of the court meant that the scrap could not be part of the bankruptcy estate because the yard was not the owner as the bankruptcy was opened.

In isolation these cases cannot give solid basis for determining the legal position of the acquirer in the bankruptcy of the disposer. But possibly one can conclude from these cases that mere agreement alone does not provide sufficient evidence to obtain perfection, it requires “something” more¹²⁹.

¹²⁴ Brækhus. S.499- 517.

¹²⁵ Lilleholt. S.192-195. Andenæs. S.184. Falkanger. S.624-625.

¹²⁶ Rg.1972.53. Rg.1963.492.

¹²⁷ Rt.1910.231.

¹²⁸ Rt..1912.263.

¹²⁹ Lilleholt. S.191.

5.3.2 The interest doctrine

The decisions in the cow- case and the iron scrap-case, as well as the arguments of the courts in these are the core in Brækhus Herrems justification of the interest doctrine¹³⁰. As mentioned it requires something that provides more evidence than the mere agreement to obtain perfection. According to these “the purchasers’ right should be protected against the seller’s creditors where the sales object is put at the disposition of the buyer, or where it only depends on the buyer when he gets possession of the contractual object. The same should probably be the case if only the transport remains, or where the seller shall perform certain extra work on the object which is actually ready for delivery”¹³¹. This view was supported in RG.1972.53 where the court pronounced, that the state of the law must be that the acquirer is protected if he “can claim to get the object delivered immediately or whenever he may wish it”. In other words these quotations express that perfection is obtained if the object is at the seller in the interest of the buyer. The political rationale behind the exemption is that when the contractual object is at the seller’s premises, in the buyer’s interest then reciprocity in the transaction is fulfilled to some extent¹³². Thereby the buyer has not granted the seller a credit performance and the buyer should not be considered among the sellers other unsecured creditors.

5.3.3 Justification for departing from the requirement of handover

The condition of handover to protect the acquirer from the disposer’s creditors is justified by the consideration to avoid creditor fraud. The handover makes the transaction evident to some extent. When the debtor is at the brink of bankruptcy, then there are usually others he would rather wish to benefit than his creditors. Then it is easy to claim that objects located

¹³⁰ Brækhus Herrem. S.499- 517

¹³¹ Quote: Brækhus. S.513.(My translation)

¹³² Brækhus. S.513.

at the debtor, at the time of the creditor seizure is sold. If handover is required it is harder to construct such acquisitions in retrospect. It should be mentioned that creditor fraud also is remedied through the avoidance rules, cf. the satisfaction of claims act chapter. 5.

Furthermore the handover requirement can be justified by the close parallel between transactions of property rights and pledges. The pledge rule follows from the mortgage act § 3-2¹³³ and handover is a requirement for perfection. In the pledge rule the handover requirement shall grant the pledge evidence as well as make it harder to encumber chattels¹³⁴. As a consequence it should not be easy to bypass the pledge requirement by camouflaging the pledge as a sale.¹³⁵ This indicates that the perfection rules for pledges and transfer of property right in chattels should be parallel. One can also argue that the handover requirement for acquisition of chattels creates better system and consistency in the creditor protection rules. As “other assets usually gains perfection through registration or notification it is not unreasonable to also require a outer statement for the acquisition of chattels”¹³⁶. Moreover, if payment is made in advance the buyer has *de facto* granted the seller a loan. Then it is reasonable to equate the buyer with the sellers other unsecured creditors¹³⁷.

There are however several considerations against the condition of handover to obtain perfection for chattels. Firstly, such condition makes it more difficult to get unsecured payments in advance. Payments in advance can in many cases be a rational way of financing¹³⁸. Secondly, the requirement of handover may lead to unreasonable results for the acquirer. This is especially relevant in cases where a consumer has paid in advance to a professional salesman¹³⁹. Moreover the evidence one achieves through handover is rather

¹³³ The mortgage act §1-1.3: A pledge is when the mortgagee or a third party holds the pledge object as security for a claim, cf. Skoghøy. S.36.

¹³⁴ Lilleholt. S.196.

¹³⁵ Brækhus. S.499-517.

¹³⁶ Lilleholt. S.193. (My translation)

¹³⁷ Brækhus. S.508.

¹³⁸ Brækhus. S.507

¹³⁹ See: 5.3.4

limited. So, if the parties really want to commit creditor fraud, then one would also be able to arrange a false handover. In this retrospect it should be mentioned that in relation to transaction of property as opposed to a pledge¹⁴⁰, the handover do not have to be permanent¹⁴¹. This is relevant because it makes it easier to arrange a false handover, thereby reducing the evidence obtained through handover, in relation to transfer of property rights in chattels.

In light of the relevant case law, the opinion of the law presented in legal theory and the relevant considerations the handover requirement is the main rule. However this requirement should not be applied more extensively than its rational require. This indicates that the acquirer should be protected in cases where the risk of creditor fraud is small¹⁴². This is the case in manufacturing contracts and purchases where a consumer pays in advance to a professional salesman.

5.3.4 Exemption from the handover doctrine in consumer contracts

As mentioned above the requirement of handover may lead to unreasonable results when a consumer has paid in advance to a professional seller. This consideration has led to a statutory exemption from the handover requirement in Swedish law¹⁴³. The main argument to interpret such a rule in Norwegian law is that similarly to manufacturing contracts the risk of creditor fraud is relatively small¹⁴⁴. As the consideration to avoid creditor fraud is the main justification behind the concept of creditor extinction, and requirement of handover should not apply more extensively than the state of its reason, this indicates that there should be an exemption from the requirement of handover in the case where a consumer has paid in advance to a professional seller. This is supported by the

¹⁴⁰ Mortgage act. §3-2.

¹⁴¹ Lilleholt. S.193-194.

¹⁴² Lilleholt. S.194

¹⁴³ Regarding the Swedish discussion see: Goranson. S.666. Konsumentkoppslag §49.

¹⁴⁴ Lilleholt. S.194

development in Norwegian law, which has moved towards interpreting rules to support the right of consumers as the weaker contracting party¹⁴⁵. Further there are already fairly extensive exemptions from the requirement of handover¹⁴⁶. This could indicate that there is an exemption from the handover requirement in cases where consumers have made a payment in advance to a professional seller.

However, the development in Norwegian law towards interpreting the rules to support the consumer as the weaker party to a contract, refer to the consumers contractual relationship with a professional seller. Then it is the consumer's weak position as a contractual party that is protected. It is more natural to include special consumer protection rules in contract law than in property law. This is because a special perfection rule for consumers would affect the seller's creditors creating an uneven distribution among them.

It is nothing that indicates that the consumer have been prioritized in the relationship to a third party creditor according to Norwegian law. Also the other exemptions from the handover requirement are based on a core understanding that has been developed in legal theory. This is also what Brækhus Herrem could retract from the cow- and Iron scrap-case: That the mere agreement alone is not enough to establish perfection. The transaction must in some way be given evidence in addition to the evidence provided through the conclusion of the contract. In this retrospect the mere consideration that the handover requirement may lead to unreasonable results, and that the risk of creditor fraud is small, are not factors that make it easier to verify that there is an actual transaction. In other words, these factors do not provide the additional required evidence. This indicates that if there should be an exemption from the handover requirement for consumer purchases in Norwegian law, it must be introduced through the imposition of a statutory rule.

¹⁴⁵ The creation of the law of consumer purchases. Rt.1998.774 (Where the question was whether there was grounds for a special burden of proof in the favor of the consumer, in consumer purchases. The supreme court said no, but the fact that the question was raised illustrates the importance in considering consumers in norwegian law)

¹⁴⁶ The interest doctrine and the exemption for manufacturing contracts. Brækhus S.499-517.

However, such a rule would weaken professional salesmen's possibility to raise credit through encumbering their inventory¹⁴⁷. This can be illustrated in that it would be even harder to determine the real content of the inventory. Furthermore, such a rule might lead to practical problems regarding individualization. For instance, whether the seller is obligated to individualize the contractual object, and what happens if this has not been done¹⁴⁸.

To summarize, there is no case law to support an exemption from the requirement of handover in the case of consumer purchases. Lilleholt argues that there should be an exemption in this case, but does not go so far as to claim there is an exemption according to the state of law¹⁴⁹. Brækhus Herrem and Andenæs on the other hand, do not even discuss whether it is an exemption regarding consumer purchases. In retrospect to Brækhus Herrem's thorough presentation of what is required for perfection in relation to chattels, there is nothing in consumer purchases that provide the additional evidence that justify the other exemptions from the requirement of handover¹⁵⁰. Furthermore, the perfection rules are not suited to protect consumers. Hence, it is not an exemption from the requirement of handover to obtain perfection in consumer purchases of chattels.

5.4 The exemption from the requirement of handover in manufacturing contracts

5.4.1 The special features of manufacturing contracts

Manufacturing contracts differ from other purchase contracts in that the buyer finances the procurements and the actual construction as it takes place through down payments. In this way the buyer is the one financing the manufacturing. The other option would be that the yard had to get the financing elsewhere. The financing would have to be in place before

¹⁴⁷ Mortgage act. §3-11 to §3-13.

¹⁴⁸ Individualisation is a requirement for any property right. Cf. Brækhus S.513-517.

¹⁴⁹ Lilleholt. S.194.

¹⁵⁰ The interest. Doctrine. CF.5.2 and Manufacturing contracts.S.5.4.

construction could begin and it would therefore be difficult for the yard to provide sufficient security. Due to this complication it is a good solution to rather let the buyer finance the construction through down payments. The manufacturing contracts are usually based on standard contracts¹⁵¹. NF 05, NKT 05 and NSF 2000 are all as a starting point based on financing through down payments.

Another typical feature of the manufacturing contracts mentioned above, is that the contract explicitly regulate the transfer of ownership to the contractual object¹⁵². Further, they regulate the transfer of ownership to materials that are to be incorporated into the contractual object. For example see NF 05 art 22.1: “The Company gain property of the contractual object as the work progresses. Materials become the property of the company when they are brought to the building site or when payment is made, that is if payment is made earlier”. It is important to mention that the inter parties agreement cannot affect the distribution in bankruptcy in relation to third party creditors. This as the rules on creditor extinction is in principle mandatory¹⁵³.

5.4.2 The exemption from the requirement of handover for manufacturing contracts

5.4.2.1 The starting point according to case law

The question is whether the buyer's right to the contractual object during construction is protected from the yards creditors despite being located at the yard.

¹⁵¹ See Chapter 2. For instance NF 05, NKT 05 NSF 2000.

¹⁵² Lilleholt. S.198.

¹⁵³ Lilleholt. S.198.

The Bomek-case¹⁵⁴ is the only case regarding this problem. In this case Bodø mek manufactured three modules for the Statfjord 3 platform. The modules were 97% finished when Bodø mek was forced to composition in bankruptcy. The court decided that the buyer had not obtained perfection in relation to the transfer of property in the modules, and could not claim to have them delivered. The court did not even consider whether there was an exemption from the handover requirement for manufacturing contracts. Instead, the court applied the interest doctrine, and as the contractual object was still situated at the yard, with some contractual work to be done, it was there in the yard's interest. Hence, the buyer had not obtained perfection for the transaction and did not have a separatist right to the contractual object. This solution is however heavily criticized¹⁵⁵ as it does not even discuss whether there is an exemption from the handover requirement for manufacturing contracts.

5.4.2.2 Theory and general considerations against an exemption from the handover requirement for manufacturing contracts

The main argument for not having an exemption from the handover requirement for manufacturing contracts is that most large manufacturing contracts can be registered in the ship building register. When the buyer has this possibility to protect his property right through registration, he should not be protected if he has chosen not to register. This is supported by the fact that large manufacturing contracts are agreements between very resourceful parties, which obviously consider security against the other party's bankruptcy. These contracts also contain special sections regarding bankruptcy security, either through registration or bank guarantee. Therefore it would not be unreasonable if the buyer were without protection, as he has chosen not to secure his down payments and/or right to the newbuilding.

¹⁵⁴ Nd.1982.264. (Bodø namsrett).

¹⁵⁵ Andenæs. S.187-188.Falkanger. S.518.Lilleholt. S.199.

On the other hand, neither Brækhus Herrem nor Andenæs assess this consideration in their discussions regarding perfection without registration in manufacturing contracts. This cannot be decisive, as this consideration is obviously very relevant in determining how this problem should be solved.

That the buyer should not be protected when he has chosen not to register should also be viewed in the light of the consideration to have clear-cut rules with systemic features and consistency in property law. If the buyer has no right to the contractual object unless it follows from the ship register, it would be easier for all parties involved with the project to predict their legal position. That property law should have clear-cut rules is supported by the statement of the Supreme Court in the Dorian Grey-case¹⁵⁶.

It should be mentioned that scholars also generally present rather few arguments opposed to an exemption from the handover requirement for manufacturing contracts¹⁵⁷. However, the only case law¹⁵⁸ on this problem indicates that there is no exemption from the handover requirement for manufacturing contracts. Even though the decision was given by a low-level court¹⁵⁹, and is heavily criticized in theory¹⁶⁰ it is clearly a valid source of law. This supports that there is no exemption from the handover requirement for manufacturing contracts.

5.4.2.3 Theory and general considerations for an exemption from the handover requirement regarding manufacturing contracts

The main argument for considering the buyer to be the owner of the manufacturing object without handover, is that it could be necessary that the buyer contributes to the financing in

¹⁵⁶ Rt.1998.268.

¹⁵⁷ Lilleholt. S.199.Andenæs. S.188.Falkanger. S.632.

¹⁵⁸ ND.1982.264.

¹⁵⁹ Bodø namsrett.

¹⁶⁰ Lilleholt. S.199. Andenæs. S.188.Falkanger. S.632.

the manufacturing phase, and that the buyer's corresponding need for security may easily be safeguarded through property right in the manufacturing object¹⁶¹. Also, there is little risk of creditor fraud in extensive manufacturing contracts. The commitments between the parties is so comprehensively regulated in the contract that it is very difficult to arrange a false transaction, in a way that would not be discovered by the bankruptcy estate afterwards. As a consequence it has been argued in theory that the evidence consideration has relatively low influence in large manufacturing contracts¹⁶². However one should rather say that the transaction gains evidence due to the system and content of the contract. Hence, there is no need for the additional evidence provided through handover. This corresponds to the core of Brækhus' discussion of exemptions from the handover requirement¹⁶³. The mere agreement alone is not sufficient for perfection¹⁶⁴. In the case of manufacturing contracts the comprehensive content and system in the contract provide the additional evidence necessary to exempt from the requirement of handover. Further, in assessing the theoretical justification behind the rule it is important to consider that the down payments give little indication of being a credit performance. This as the down payments is used to finance materials and the actual construction as it progresses, and without the buyer's down payments, this would otherwise be financed by the yard through a loan. This indicates that reciprocity in the contractual relationship is achieved to some extent. As the buyer is not in fact granting the yard with a credit performance through his down payments it is unreasonable that he is considered equally to the yards other unsecured creditors¹⁶⁵.

5.4.2.4 The state of the law

¹⁶¹ Andenæs. S.186.

¹⁶² Andenæs. S.186

¹⁶³ Brækhus. S.499-518.

¹⁶⁴ Lilleholt. S.191.

¹⁶⁵ Brækhus. S.510

In current law it is relatively obvious that there is an exemption from the handover requirement for manufacturing contracts. That the legal basis for this exemption is mere theory must be considered sufficient because these theories have a solid foundation in legal theory, and have extensive support in the considerations that are relevant today.

5.4.2.5 The extent of the exemption from the handover requirement for manufacturing contracts

The buyer is owner of the contractual object as soon as it can be individualized. The property right extends to what can be considered the contractual object at any time during the construction. This is parallel to the solution if the buyer is registered as owner of the newbuilding, and art 22 of NF 05. Further the extent of the buyer's right must be assessed in relation to his right to materials, parts and equipment.

5.4.3 Whether the exemption for manufacturing contracts extends to materials, parts and equipment

5.4.3.1 Introduction

Regarding parts, equipment and materials that are situated at the yard, but are not yet incorporated into the contractual object it is more complicated. When the buyer finances the construction through down payments, it is clear that the first payments to a large extent will be used to purchase materials and parts to be incorporated into the contractual object. Therefore, the buyer's need for protection may be just as important in relation to materials, as to the contractual object itself. On the other hand there are greater concerns regarding the buyer's separatist right to the materials than to the contractual object itself¹⁶⁶. As most

¹⁶⁶ Brækhus. S.511.

yards build several ships at the same time, they have materials purchased for each individual project as well as a more general storage of materials that are used for all projects where it seems to fit. In relation to ownership this could be rather complex, and in case of bankruptcy the possibility of creditor fraud is definitely present¹⁶⁷.

5.4.3.2 Materials provided by the buyer

Materials that are purchased by the buyer are never the property of the yard, even though they are brought to the yard. As a consequence the yard's creditors cannot claim these materials¹⁶⁸ in a bankruptcy situation.

5.4.3.3 Materials provided by the yard

Regarding materials purchased by- and brought to the yard it may be a conflict in relation to the yard's creditors. What belongs to newbuilding no 1, and what belongs to newbuilding no 2. In relation to security interests there are relatively simple identification measures for materials situated at the yard, cf. § 41, cf. MC § 43. The registered pledge includes materials and equipment for the ship which "through marking or in another reassuring way is identified for incorporation"¹⁶⁹. For example to paint the construction number on the steel plates will thereby be sufficient.¹⁷⁰

Regarding property right in relation to the exemption from the requirement of handover and in relation to registration, the same requirement of marking or other reassuring identification should apply¹⁷¹. The buyer gains property right to the materials when they are

¹⁶⁷ Brækhus. S.511.

¹⁶⁸ Falkanger. S.632.Kaasen. S.539.

¹⁶⁹ MC §43. (My translation)

¹⁷⁰ Falkanger. S.632.

¹⁷¹ Falkanger. S.632.Andenæs. S.186.Lilleholt.S.199

brought to the yard. However, Bræhus argue that in addition to reassuring identification the buyer's property right in the materials should follow from expressed agreement, as well as how the reassuring identification shall be indicated¹⁷². A requirement of expressed agreement would make it harder to forge reassuring identification in the critical time prior to bankruptcy, and thereby reducing the risk of creditor fraud.

Presentations by recent scholars have not mentioned express agreement as a requirement for perfection regarding parts and materials¹⁷³. However, a provision regarding the property right to parts and materials are included in both NF 05 and NSF 2000. A requirement of express agreement would provide evidence in relation to the extent of the buyer's right in the materials situated at the yard. Thereby reducing the risk of creditor fraud.

On the other hand, to introduce yet another requirement to establish perfection regarding ownership to materials would make the rules unnecessary complicated. The Supreme Court addressed this question in an *obiter dicta* statement in Rt.1990.59. Myra båt-case. The case was regarding real property construction, but as construction is a specific type of manufacturing contract the statement could be relevant also to ship building and petroleum construction contracts. It was stated that: "It can be questioned whether it should not be the general rule in manufacturing contracts – even though there are no express agreement – that the buyer gains property right to materials that are brought to the building site, when the value of these materials together with the work that has been performed, is within the total sum of the buyer's down payments so far". This indicates that express agreement is not required to obtain perfection in relation to materials situated at the yard.

However, one can argue that there are substantial differences between real estate construction and yard construction. Firstly, there is a significant difference between real estate construction and yard construction because there are usually several ships and/or platforms under construction at a shipyard. As a consequence, it may be uncertainty as to

¹⁷² Bræhus. S.512.

¹⁷³ Falkanger. S.632.Andenæs. S.186.Lilleholt.S.199

which materials belong to which project. This indicates that there is a significant risk of creditor fraud in relation to materials as opposed to the contractual object itself. On the other hand, it does not matter whether the materials belong to ship A or ship B, as long as it is known that the materials do not belong to the yard and thereby is not the subject to the bankruptcy estate. Still, the yard usually has materials that are bought to be used in several projects. When there are materials from several projects and others, which are not tied to any project located at the yard at the same time, the risk of creditor fraud is obviously higher than in real estate construction, where this is not the case.

Furthermore, there is an obvious difference in relation to property right in real estate construction as opposed to yard construction, as the buyer owns the construction site. In real estate construction the transfer of ownership to materials is more clearly expressed as the materials arrive at a place owned by the buyer. The parallel to the handover requirement for ordinary transactions is closer when the materials are actually delivered to the buyer as opposed to be delivered at the yard. This indicates that the supreme courts *obiter dicta* in the Myra båt-case cannot be transferred to yard-construction contracts generally, and supports the requirement of express agreement to obtain perfection for materials.

However, the difference in delivering the materials to a building site owned by the buyer rather than the yard do not provide any additional evidence in relation to the transfer of ownership. This as the actual transfer of the materials to the yard is just as verifiable regardless who owns the building site. Further the *obiter dicta* explicitly question whether the statements constitute a general rule for manufacturing contracts. Even though there is a considerable difference between land manufacturing and yard manufacturing, the contracts are very similar and should if possible follow the same mandatory framework. As a consequence the statement in the Myra båt-case must be understood as being applicable to all manufacturing contracts¹⁷⁴. This understanding is supported in theory¹⁷⁵. There is no

¹⁷⁴ Kaasen. S.540.

¹⁷⁵ Falkanger. 632. Andenæs. S.186. Lilleholt. S.199

requirement of express agreement to obtain perfection for materials. Perfection is obtained if the materials are marked, or in another way reassuringly identified.

5.4.3.4 Whether the buyer have a separatist right to materials and equipment that is still located at the yards supplier

In manufacturing contracts, especially in large projects regulated by NF 05 it is common for the yard to delegate some of their work to suppliers¹⁷⁶. A question that arises is whether the buyer has a separatist right to the materials and equipment that is still located at the yard's supplier.

An exemption from the requirement of handover for perfection in relation to materials situated at the yard's supplier would be based on an extension of the non-statutory perfection rule regarding materials and equipment located at the yard. One could view this as the buyer getting a protected right to the yard's claim against his supplier¹⁷⁷. But if the buyer should get a protected right in the claim, then the claim must be conveyed to him according to the debentures act § 29.1¹⁷⁸. As this transport cannot be presumed¹⁷⁹, this view cannot be the general basis for granting the buyer protected right in materials located at the yard's supplier.

One can also approach the problem by questioning whether the buyer gets property rights directly in the materials parallel to the yard's rights in the materials. It can be argued that this would be to bend the buyer's protection too far in relation to the main rule of handover as a requirement for perfection. On the other hand, the risk of creditor fraud is not any greater than if the materials are located at the yard.

¹⁷⁶ NF.05.art.8.

¹⁷⁷ Lilleholt. S.199.

¹⁷⁸ The debenture act §29.1 formally only apply for non-negotiable promissory notes but after Rt.1957.778 it also apply for other simple claims.

¹⁷⁹ Brækhus. S.512.

In legal theory, it is assumed that to grant the buyer a protected right in materials that are still located at the yards supplier would depart too much from the main requirement of handover to obtain perfection¹⁸⁰. The buyer's right to specific performance of materials still located at the yard's supplier is rather protected by NF 05 art 22.3 which states that the yard shall make sure the buyer can register property rights in sub- deliveries in the ship building register. Thereby avoiding the problem altogether.

5.5 The situation where neither payment or handover have taken place at the time of the bankruptcy/creditor seizure

According to the previous discussion in this chapter, the starting point was that the buyer had paid in advance. Therefore it is principally a very different conflict if neither payment nor handover have been completed, at the time of the creditor seizure/bankruptcy. In this situation some scholars argue that there is no conflicting interest at all, as long as the payment, according to the agreement is on more or less normal terms¹⁸¹. The seller's creditors will seldom oppose that the buyer gets the contractual object against paying the purchase sum. However there could still be conflict, for instance if there is a rise in the market value.

Brækhus argue that the buyer is always entitled to the contractual object in return for paying the purchase sum¹⁸². The main justification in his reasoning is that the requirement of handover is meant to separatist genuine transactions from mere credit performances. Hence, when there is no credit performance in consideration, it is reasonable to allow the buyer specific performance against paying the purchase sum¹⁸³. However, if the buyer is

¹⁸⁰ Andenæs. S.187.Brækhus. S.512.

¹⁸¹ Boarder towards gifts or gift sales. Perfection for gifts require handover, cf.Rt.1988.1327. This as the risk of creditor fraud is especially big in relation to gifts.

¹⁸² Brækhus. S.508.

¹⁸³ Brækhus. S.508, 513, 514.

entitled to specific performance, he is also entitled to get any dispute regarding the content of the purchase contract resolved legally. The consideration of the bankruptcy estate indicates that they should be able to exercise their right of seizure without being forced into such dispute¹⁸⁴. In other words they should be able to freely disposed over the contractual object. This rationale is the same as regarding the bankruptcy estate's right to choose whether they want to enter the debtor's contracts or not¹⁸⁵, and is justified in the consideration to ensure effective bankruptcy proceedings¹⁸⁶. Further the buyer is in a far more remote relationship to the contractual object if he has not paid the purchase sum. As a consequence the consensus in legal theory today is that the buyer does not have perfection for his right to specific performance, even if he agrees to pay the agreed purchase sum¹⁸⁷.

6 Conclusion

Through presenting the typical features of bankruptcy protection in large manufacturing contracts and the perfection rules of registration in the register of ships, I have illustrated the relevance of the problem of the thesis. The registration option in MC § 31 is an unpredictable and complicated rule, which is not in line with the system and consistency in property law.

The main question was whether one could apply the perfection rules for chattels, if the option to register the contract has not been used.

¹⁸⁴ Andenæs. S.185.

¹⁸⁵ Cf. Satisfaction of claims act. §7-3.

¹⁸⁶ NOU.1972;20

¹⁸⁷ Andenæs. S.185.Lindbrække. S.212.Falkanger. S.509.

I assessed this indirectly by questioning whether the buyer's right to the contractual object during construction is a security interest, cf. SCA § 1-1.1. In this discussion the relevant factors were; the purpose of the buyer's right, and the buyer's real right of disposition. Through a comprehensive discussion I discovered that the buyer in reality had no right of disposition beyond the right to cover his claim in the contractual object. Therefore the buyer's right must be considered a security interest according to the mortgage act § 1-1.1. As the buyer's right to the contractual object is a security interest, it must be registered to have perfection, cf. MC § 41 and thus, blocking the exemption from the handover requirement in manufacturing contracts.

As legal theory do not support the buyer's right being a security interest, I also performed a more general discussion of whether the perfection rules apply if the registration option has not been used. The relevant factors were the close relationship to pledges, the option to register and the statements of the maritime law comity in relation to MC § 31. When MC § was created it was clearly not the intention of the legislator to change the perfection rules. Hence, the perfection rules for chattels apply.

But, as the buyer's right in the contractual object should be considered a security interest, MC § 41 is effectively blocking the application of the perfection rules for chattels, resulting in that the buyer has no perfected right in the contractual object without registration. Viewing the characteristics of the manufacturing contracts, the perfection rules of registration and the perfection rules for chattels, in light of the importance of system and consistency in property law, I have concluded that this solution would also be preferable in a *de lege ferenda* perspective.

With the starting point that the handover requirement should not apply further than its reason, I did a thorough review of the considerations for and against a requirement of handover in the perfection rules for chattels. I have discovered the relevant factors in determining whether the buyer is protected in the yard's bankruptcy in manufacturing contracts, and how these should be weighted. These are mainly the consideration to avoid

creditor fraud, the consideration of system and predictable rules in property law and the yard's need for financing the construction with the buyer's corresponding need for security. Based on these factors there is obviously an exemption from the handover requirement to obtain perfection in chattels for manufacturing contracts. Moreover this solution has extensive support in theory.

References

List of Judgements/Decisions

Rt. 1935.981 (Byggland)
ND. 1982.264 (BOMEK)
Rt. 1998.268. (Dorian Grey)
Rg. 2003.514
Rt. 1995.205
Rt. 1996.918
Rt. 1993.565 (Ofoten)
Rt. 1910.231 (The cow-case)
Rt. 1912.263 (The Iron scrap-case)
Rg. 1972.53
Rg. 1963.492
Rt. 1998.774
Rt. 1988.1327

Treaties/Statutes/contracts

The Norwegian satisfaction of claims act. 1984. Nr. 59
The Norwegian maritime code. 1994. Nr. 39
The Norwegian land registration act. 1935. Nr. 2
The Norwegian mortgage act. 1980. Nr. 2
The Norwegian NIS act. 1987. Nr. 48
The Norwegian debenture act. 1939. Nr. 1
The Swedish act of consumer purchases.

NSF 2000

NF 05

Secondary Literature

Brækhus Herrem. Tingsrett. 1964. 2 ed.

Lilleholt. Legitimasjon, publisitet og notoritet. (JV-1996-69)

Lilleholt. Godtroerverv og kreditorbeslag. 1999. 3 ed.

Arnholm. Alminnelig privatrett. 1964. 1 ed.

Kaasen. Petroleumskontrakter. Kommentar til NF 05 og NKT 05. 2006.

Andenæs. Konkurs. 1999. 2 ed.

Meland. Kommentar til Norsk standard skipsbyggingskontrakt. 2006. 1 ed.

Knutzon. Nordisk medlemsblad. 1984.nr. 17

Bull, Falkanger, Brautaset. Scandinavian maritime law. The norwegian perspective. 2008.
2 ed.

Martiniussen. Hevd som rettsvernsurrogat. (JV-2003-264)

Gyldendal rettsdata. Kommentar til MC Chapter 2. Falkanger.

Selvig. 1982 s. X111.

Kruger. Bestillerens rettsstilling.

Falkanger. Tingsrett. 2007. 6 ed.

Skoghøy. Panterett. 2008. 2 ed.

Goranson. Tradisjonsprinsippet. Swedish.

Lindbrække. Eiendomsrett og konkursbeslag. 1946. 1 ed.

FOR.1987-06-26. Nr. 554

Ot. Prp. Nr. 41 (1991-1992)

Op. Prp. 1980.110

NOU.1972;20

